

**New Mexico Taxation & Revenue Department
Film Production Tax Credit
Certified Public Accountant Audit Agreed Upon Procedures**

I. Introduction

The New Mexico Film Tax Credit was created for an eligible Film Production Company. The purpose of the certified public accountant (CPA) audit is to ensure and verify the qualified expenditures incurred when producing qualified motion pictures in New Mexico and has complied with the requirements that became effective July 1, 2011.

The tax credit is refundable and can be used to offset either New Mexico personal or corporate income taxes and/or other taxes.

The following audit agreed upon procedures (AUP) is a helpful guideline relate to the requirements as stated in Section 7-2F-2.1 (A) NMSA 1978 states and : "...If the amount of the requested tax credit exceeds five million dollars (\$5,000,000), the application shall also include the results of an audit, conducted by a certified public accountant licensed to practice in New Mexico...."

II. Statutory References

Section 7-2F-1 (T) NMSA 1978, that commence principal photography prior to January 1, 2016.

Section 7-2F-2.1 (A) NMSA 1978, that commence principal photography on or after January 1, 2016.

III. Guideline for Production Company

A. Selection of the Certified Public Accountant (CPA).

The audit **must** be performed by a CPA licensed to practice in New Mexico (NM).

The audit **must** include a copy of the CPA's license to practice in NM and a notarized statement confirming the CPA is independent from any other activities related to the film project for which is being audited. Prior approval of CPA selection is not required from the New Mexico Taxation and Revenue Department (TRD).

The following Report and Workpapers submitted by the CPA must include the following information:

1. The CPA's name, address, and telephone number.
2. The name of the Production Company and project name.
3. The date that the agreed upon procedures were completed.

The production company's cost information must be presented in U.S. dollars.

The expenditure for a required external audit by CPA licensed to practice in NM is eligible if the CPA has physical presence (bricks and mortar) and services are rendered in-state. Accrued amounts (e.g. a flat fee) or hourly invoices are both acceptable forms of payment. The application would have to be submitted, and the expenditure paid, on or after June 19, 2015.

A. Scope and Objective of the Audit

The Department defines "CPA Audit" as the phrase is used in Section 7-2F-2.1 (A) NMSA 1978, as agreed upon audit procedures.

The CPA will conduct the review with AUP of the production's records to ensure the production company is in compliance with the requirements stated in Section 7-2F-2.1 (A), for film production tax credit application over \$5 Million.

The production company must confirm the expenditures claimed on the Pre-Submission Worksheet were incurred during the production company's tax year.

IV. Agreed Upon Procedures

TRD will assign an auditor to communicate with CPA for any questions and to verify New Mexico residency, entities and/or questionable transactions.

The production company shall provide the CPA with selected samples of NM expenditures pull by TRD and **complete** bibles (ledgers, not part of samples).

PLEASE REFER TO:

- ***NEW MEXICO REFUNDABLE FILM PRODUCTION TAX CREDIT - SUBMISSION OF BIBLES (LEDGERS)***
- ***NEW MEXICO REFUNDABLE FILM PRODUCTION TAX CREDIT – QUALIFYING AND NON-QUALIFYING EXPENDITURES***

Documents can be found on the following website:

<http://www.tax.newmexico.gov/Tax-Professionals/film-production-tax-credit.aspx>

Expenditures (excluding payroll)

1. The CPA will ensure compliance with the requirements of Section 7-2F-2.1 (A) NMSA 1978, film production tax credit and follow the guidelines for submission as set forth by TRD and the New Mexico Film Office (NMFO).
2. Verification procedures are to be followed for accounts payable, petty cash, journal entries, credit card and fuel card expenditures as identified.
3. For each expenditure item selected in a sample (if there is enough items of interest) , perform the following procedures:
 - a. Inspect invoices and cancelled checks, receipts or other equivalent documentation. Verify that the expenditure is taxable in NM and the amount is correct, incurred and paid for services rendered and/or goods used in NM.
 - b. Verify that the expenditure is an allowable cost (refer to statute, regulations and the NM qualifying and non-qualifying expenditures).
 - c. Ensure vendor's name and FEIN, SSN, or NM CRS number is identified and information in note column on the worksheet.
 - d. Inspect vendors and ensure that physical presence is met in NM by working with auditor assigned.
 - e. Verify shipping expenditures originate in NM.
 - f. Verify internet purchases are shipped to a NM Vendor and is taxable.

Example: Staples purchased on line and shipped to an NM location. Receipt will have NM location and gross receipts tax.

- g. Verify insurance coverage and bonding is purchased through a NM based Insurance Agent or Broker.

- h. Inspect invoices and cancelled checks, receipts or other equivalent documentation on the high dollar expenditure's **(detailed transactions not included in the sample)** that are taxable and the amount is correct, incurred and paid for services rendered and/or goods used in NM.
- i. Verify commercial airline flights are purchased through a NM based travel agent or Travel Company and originates or arrives in NM or within NM that is directly attributable to production.

Example: Overseas to NY to Albuquerque. If the individual stays a couple of days in NY, the flight from NY to Albuquerque would **only** be eligible for the incentive.

Verify payments to a NM travel agent for baggage fee on airline flight, transportation from a NM airport and/or other services that are provided and/or preformed in NM.

- j. Limitation on car rentals/leasing, gifts, artwork or jewelry on set, and hotels (refer to statute, regulations and the NM Chart of Accounts).
- k. Verify that the expenditure was recorded net of any refunds, discounts, rebates, invoicing errors, and purchase returns, as recorded in the general ledgers.
- l. Verify that the expenditures were recorded net of proceeds from any item of production sales.
- m. Verify and disallow expenditures on Native American entities on Indian reservations, non-profit entities, out of state vendors with no physical presence in NM (refer to statute and regulations), government entities and entertainment (events, wrap parties, etc.).
- n. **In its own tab: Extras (Background)** – Employee's Full name and social security, job title - Total wages, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased for a NM based agent or broker).

 **An individual with an out-of-state address is to be disallowed.**

- 4. Obtain a listing from the production company of assets which were not destroyed in the process of the making of the production and that are being held for future productions or other purposes.

Submit the Schedule of Retained Assets based on the list provided by the Production Company and documentation (picture) of assets that were destroyed in the film production process as an attachment to the AUP Report.

For all fixed assets on the listing perform the following procedures:

- a. Verify the cost of the item if the cost is greater the item would then be amortized post-production or effects equipment, including but not limited to computers, hardware and relevant components, printers and copiers being held for future productions or use were included as a qualified expenditure, (and were identified as such in the GL reports).
- b. For all other assets, all sales on qualified expenditures, (such as props, customs, etc.) are to be subtracted from the assets.
- c. Verify invoice for any asset that is destroyed during production and included documentation (picture) identifying what happened to the asset after the production wrapped.

Payroll Expenditures

Payroll ledgers reconcile with Payroll Company's Full Detail Earning Report.

Payroll ledgers to be submitted by each categorize in its own individual tab and must reconcile with Payroll Company's Detail Earning Report also categorized in its own individual tab.

- Master
- Summary
- NM Crew
- NM Cast
- Non Resident Crew Exceptions (NRCE-Specialty Hires)
- Non Resident Crew
- Direct Hires (Actors directly hire by production company.)
- Super Loan Outs (SLO)

New Mexico Crew and Cast

Full Name and Social Security (only) of **resident New Mexico**: Crew and Performing Artists, both full-time and first year residents.

Master Bible – complete information of all categorizes

Summary total per category: New Mexico Crew \$ amount, New Mexico Performing Artists \$ amount, NRCE \$ amount, Non-Resident Crew \$ amount, Direct Hires \$ amount, Super Loan Out \$ amount and Extras (Background) \$ amount.

New Mexico Crew Bible – Employee's Full name and social security, job title - Total salaries, and wages, kit rentals, per-diem, pension, health & welfare, vacation, holiday, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased for a NM based agent or broker).

New Mexico Performing Artists Bible - Employee's Full name and social security, job title - Total salaries, and wages, kit rentals, per-diem, pension, health & welfare, vacation, holiday, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased for a NM based agent or broker).

Non Resident Crew and Cast

Non-Resident Crew Exceptions (NRCE) - Employee's Full name, social security, job title - Total wages (earning, vacation & holiday), fringe benefits (pension, health & welfare) per-diem, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased for a NM based agent or broker).

As of January 1, 2016, NRCE Program establishes a flat 15% credit of the payment of wages, fringe benefits and per-diem on employed NRCE. The amendments eliminates the need to contract a services company to employ these individuals; it eliminates Film Office from approving positions; and, it still excludes nonresident Writer, Director, Producer, Production Designer, DP, LP, Costume Designer, Still Unit Photographer and Drivers (Solely driving).

Submit spreadsheet of NRCE names and positions to NMFO for approval, upon receipt of the FTCA for film production tax credit and review of the project's New Mexico budget.

Non-Resident Crew - Employee's Full name, social security, job title - per-diem, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased for a NM based agent or broker).

Direct Hires and Loan Out Companies

➤ **FILM CREDIT PRESENTATION FOR NON-RESIDENT PERFORMING ARTIST**

PLEASE REFER TO:

<http://www.tax.newmexico.gov/Tax-Professionals/film-production-tax-credit.aspx>

Non-Resident Performing Artists Bible (Direct Hires) - Employee's Full name and social security, job title Wages, NM withholding, per diem, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased from a NM agent or broker).

For non-resident on-camera actors and stunt individuals on production payroll that NM State withholding tax is deducted and remits the first day of services rendered in NM. Regardless of exemptions claimed or number of days worked in NM.

For services rendered in NM, NM withholding tax is to be withheld at the maximum rate pursuant to the Withholding Tax Act for NM Film Tax Credit Incentive.

Super Loan-Out (SLO): Performing Artist Paid Via Super Loan Out - Employee's Full name and social security, job title Wages, Gross Receipts Tax (GRT), NM withholding, per diem, allowance, handling fee (if payroll is processed in NM) and workers' comp insurance (for individuals worked in NM if insurance is purchased from a NM agent or broker).

Invoices to be provided for SLO and confirmation that the GRT and NM withholding has been submitted to TRD.

☞ **For the purposes of this incentive, the payroll company usually can supply supporting documents to confirm GRT and Withholding was deducted and remitted.**

NOTE: All fringes on the bible are to state what it is (handling fee, FICA, SUTA, etc.) and employee's name the transaction belongs too. All payroll taxes are not eligible for tax incentive.

Workers' Comp. Insurance

If the workers' comp. insurance policy is purchased through a NM based insurance agent or broker, and employees are covered by the insurance coverage while working in NM. Yes it is direct production expenditure; therefore, the transaction is subject to tax and is rebate able.

When an employee of a production company works out of state, the transaction is not taxable in NM and not a NM direct expenditure; therefore, the workers' comp. is not rebate able.

V. Post Production Expenditures

1. Verify expenditures are for the following: Editing, Foley recording, automatic dialogue replacement, sound editing, special effects, including computer-generated imagery or other effects, scoring and music editing, beginning and end credits, negative cutting, soundtrack production, dubbing, subtitling or addition of sound or visual effects.
2. Verify postproduction expenditures made in New Mexico are as follows:
 - (a) Are directly attributable to the production of a commercial film or audiovisual product.
 - (b) Are for services performed in New Mexico.
 - (c) Are subject to taxation by the state of New Mexico.

VI. Components of the Audit

☞ PLEASE REFER TO:

➤ **NEW MEXICO REFUNDABLE FILM PRODUCTION TAX CREDIT SUBMISSION OF BIBLES (LEDGERS)**

The CPA's draft report is to indicate the outcome of the review as stated in **APPENDIX B**.

VII. FOR SUBMISSION BY PRODUCTION COMPANY TO TRD, PLEASE REFER TO:

NEW MEXICO REFUNDABLE FILM PRODUCTION TAX CREDIT - SUBMISSION OF BIBLES (LEDGERS)

NEW MEXICO REFUNDABLE FILM PRODUCTION TAX CREDIT – QUALIFYING AND NON-QUALIFYING EXPENDITURES

Documents can be found on the on the following website:

[HTTP://WWW.TAX.NEWMEXICO.GOV/TAX-PROFESSIONALS/FILM-PRODUCTION-TAX-CREDIT.ASPX](http://www.tax.newmexico.gov/tax-professionals/film-production-tax-credit.aspx)

1. TRD employee (supervisor or auditor) with the Film Tax Credit Unit will send Production Company a secure link to **upload Bibles (ledgers)**.
2. Reconcile bibles to Pre-Submission worksheet.
3. If there is more the one tax year, please submit workbooks separate titled the taxable year.
4. The auditor will run a sample utilizing the 2011 version of the Multi-State Tax Commission (MTC) sampling software to randomly select three strata's of a minimum of 75 items of interest per strata from the data provided for the qualifying period. Please refer to documents above for additional details.

FOR FINIAL SUBMISSION BY PRODUCTION COMPANY TO NMFO:

5. Film Tax Credit Application RPD 41229 (project was produced prior to January 1, 2016) or RPD 41381 (project was produced on or after January 1, 2016).
6. NMFO will submit to TRD Second Memo with Film Credit Application and the "Draft" "...results of the audit..." (As per Statute).

FOR FINIAL SUBMISSION BY PRODUCTION COMPANY TO TRD:

8. Application is entered into queue with a 180 day deadline from the date of delivery of the second memo.
9. TRD will submit links to Production Company and/or CPA to upload workpapers and the "Draft" "...**results of the audit...**" (As per statute)

- ✓ The audit **must** include a copy of the CPA's license to practice in NM.
 - ✓ A notarized statement confirming the CPA is independent from any other activities related to the film project for which is being audited.
10. TRD Supervisor and/or auditor will do their best to complete credit review at the unit level within 60 to 90 days.
- ✓ When there is constant communication with CPA and auditor.

Questions in regard to the CPA audit procedures on claiming the film production tax credit. Please contact:

Priscilla Castro
Film Tax Credit Supervisor
Taxation & Revenue Department
Audit & Compliance Bureau
Albuquerque Office (505) 841-6338
Santa Fe Office (505) 827-0919
priscilla.castro@state.nm.us

NOTE: TRD reserves the right to request additional information and documentation when reviewing the CPA's report and workpapers.

APPENDIX A

AUDIT SAMPLING:

For efficiency, the New Mexico Tax & Revenue Department (TRD) utilizes the 2011 version of the Multi-State Tax Commission (MTC) sampling software to randomly select a minimum of 75 items of interest per strata from the data provided for the qualifying period.

All samples are selected randomly using the MTC software random number generator using a seed number. The 9-digit seed number is provided by the MTC software. The seed number is documented to allow the expansion or regeneration of the sample if necessary.

AS APPLIES TO PETTY CASH: Negative and zero dollar amounts are not directly sampled; however, it is possible to reduce or eliminate a debit or credit error from the sample if a negative item reduces, cancels, or voids the same transaction included in the sample.

The sample pulled from the list will not include negatives if the company chose not to match and remove them.

The software will only pull positive transactions for to examine.

TRD auditor will test the frequency and rate of transactions that were not allowable.

This will be used to project a percentage of error on the population.

TRD auditor will consider any item that was not allowable as an error even if it was subsequently returned. The test is to see how often transactions that are not allowed are included. Subsequently returning a particular item that was tested does no change the fact that TRD have documented that the taxpayer has transactions included that should not be included.

The sample consists of the following:

Summary
Frame
Sample
Detail

Note: The sample pages may be used as workpapers.

DETAILS OF SAMPLING FRAME

1. The Taxpayer's information is entered in Multistate Tax Commission Sampling Software, Version 2011.
2. A workbook is selected.
3. The Excel data is sampled: the sample size is seventy-five (75) for each stratum.
4. Up to three strata will be part of sample for each workbook.
5. The estimated Error Rate is six percent (6%).
6. Excel Data Sampling – Stratified Frame –CRSF Unequal:
It will create a sample documentation file that is a similar format to the Excel data sampling module.
7. Summary of Sample Process:

Example:

| | \$ From | \$ To | Count | \$ Amount |
|----------------------------|-------------|----------------|--------|--------------|
| All Records | (3,500.00) | 121,500.00 | 14325 | 9,086,816.83 |
| Negatives & \$0 | (3,500.00) | 0.00 | 10 | (9,713.46) |
| Below Floor | N/Av | | | |
| Above Ceiling | 5,000.01 | 121,500.00 | 298 | 3,637,079.36 |
| Floor to Ceiling | 0.01 | 5,000.00 | 14,017 | 5,459,450.93 |
| | Floor (Low) | Ceiling (High) | | |
| Stratum | | | | |
| 1 | 0.01 | 349.99 | 9,678 | 1,035,284.41 |
| 2 | 350.00 | 1,299.99 | 3,457 | 2,301,210.37 |
| 3 | 1,300.00 | 5,000.00 | 882 | 2,122,956.15 |
| | | | | |

Above the ceiling (298 line items) will be detailed.

The population (items of interest) may be divided, by amount, into several strata and could also include items to be individually reviewed (e.g. if the item is over \$500.00). This is to reduce the overall variation of the sample. The procedure for determining the exact number of sampled stratum and stratum breaks will be determined mathematically according to a procedure explained in the sampling plan. The sample size will be approximately 75 items of interest per strata plus the detail items to be individually reviewed. A minimum of three errors per strata is necessary for extrapolation to strata population for a percentage of error (POE).

There are three rules used for extrapolating:

1. The numerator should be the sample representation of what the auditor is trying to determine about the population (or strata).
2. The denominator should be the sample representation of the population (or strata).
3. The population should be complete and should not include items that do not represent the population as defined by the test.

APPENDIX B

CPA's Independent Auditor's DRAFT REPORT ON APPLYING AGREED-UPON PROCEDURES

The following report must also include the following:

1. Introduction
2. Eligibility
 - a. Expenditures (Excluding Payroll)
 - i. State the procedures used.
 - ii. State the results of exceptions and conclusions.
 - iii. Show the results of the findings.

Example:

| Expenditure Item | Stratum | Amount in the Stratum | Sample Total | Number of Errors | Amount of Errors | Amount in the Population | Projected Errors (a) |
|-------------------------|---------|-----------------------|---------------|------------------|------------------|--------------------------|----------------------|
| <u>Accounts Payable</u> | | | | | | | |
| \$25-\$119.99 | 1 | \$ 68,248 | \$ 4,602 | 5 | \$ 369 | \$ 68,248 | \$ 3,982 |
| \$120-359.90 | 2 | 105,138 | 14,986 | 2 | 276 | 105,138 | 276 |
| \$360-\$4,000 | 3 | 123,681 | 38,654 | 6 | 3,451 | 123,681 | 8,561 |
| Greater \$4,000 | | <u>9,898</u> | <u>9,898</u> | <u>1</u> | <u>5,600</u> | <u>9,898</u> | <u>5,600</u> |
| | | <u>306,965</u> | <u>68,140</u> | <u>14</u> | <u>9,696</u> | <u>306,965</u> | <u>18,419</u> |
| <u>Petty Cash</u> | | | | | | | |
| \$25-\$119.99 | 1 | \$ 68,248 | \$ 4,602 | 5 | \$ 369 | \$ 68,248 | \$ 3,982 |
| \$120-359.90 | 2 | 105,138 | 14,986 | 2 | 276 | 105,138 | 276 |
| \$360-\$4,000 | 3 | 123,681 | 38,654 | 6 | 3,451 | 123,681 | 8,561 |
| Greater \$4,000 | | <u>9,898</u> | <u>9,898</u> | <u>1</u> | <u>5,600</u> | <u>9,898</u> | <u>5,600</u> |
| | | <u>306,965</u> | <u>68,140</u> | <u>14</u> | <u>9,696</u> | <u>306,965</u> | <u>18,419</u> |
| Grand Total | | \$613,930 | \$135,280 | 28 | 19,392 | \$613,930 | \$36,838 |

iv. Results of Extras (background).

3. Fixed Assets

- a. State the procedures used.
- b. The list of fixed assets.
- c. Results of fixed assets.

4. Journals Entry

- a. State the procedures used.
- b. Results of journal entries.

5. Payroll Expenditures

- a. State the procedures used for each category.
- b. Results of per category.

Payroll ledgers reconcile with Payroll Company's Full Detail Earning Report.

Per the Sorted Worksheet

| | Amount Claimed | Exceptions per Result |
|---|-------------------|--------------------------|
| Master -Payroll Company Report | \$ 29,748,523 | |
| Summary of all worksheets | | |
| NM Crew | \$ 10,824,509 | \$ 2,595,564 |
| NM Cast | 261,225 | 56,000 |
| Non Resident Crew Exceptions | 2,005,654 | 65,450 |
| (NRCE-Specialty Hires) | 104,354 | 104,000 |
| Non Resident Crew | 958,521 | 8,821 |
| Direct Hires (Actors directly hire by production company.) | | |
| | <u>15,594,260</u> | <u>10,000</u> |
| Super Loan Outs (SLO) | | |
| | \$ 29,748,523 | \$ 2,839,835 |
| Grand Total | | |

6. Results of non-qualified items identified (Exhibit 1)

7. Overall conclusion.

EXHIBIT 1**NON-QUALIFIED ITEMS IDENTIFIED**

| ACCOUNTS PAYABLE | | | | | | | | | |
|-------------------|---------------------|---------|------|-----------------------|-------------------|-----------------|-------------------|-------------------|----------------------|
| ACCOUNT NUMBER | REFERENCE NUMBER | STRATUM | DATE | TRANSACTION NUMBER | INVOICE NUMBER | VENDOR/EMPLOYEE | AMOUNT CLAIMED | AMOUNT ALLOWED | AMOUNT DISALLOWED |
| | | | | | | | | | |
| TOTAL | | | | | | | | | |

| PETTY CASH | | | | | | | | | |
|-------------------|---------------------|---------|------|-----------------------|-------------------|-----------------|-------------------|-------------------|----------------------|
| ACCOUNT NUMBER | REFERENCE NUMBER | STRATUM | DATE | TRANSACTION NUMBER | INVOICE NUMBER | VENDOR/EMPLOYEE | AMOUNT CLAIMED | AMOUNT ALLOWED | AMOUNT DISALLOWED |
| | | | | | | | | | |
| TOTAL | | | | | | | | | |

| PAYROLL | | | | | | | | |
|-------------------|-------------------|---------------------|-----------------------|-----------------|--|-------------------|-------------------|----------------------|
| ACCOUNT NUMBER | INVOICE NUMBER | WEEK ENDING DATE | TRANSACTION NUMBER | VENDOR/EMPLOYEE | | AMOUNT CLAIMED | AMOUNT ALLOWED | AMOUNT DISALLOWED |
| | | | | | | | | |
| TOTAL | | | | | | | | |